

Why have a Productivity Commission?

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The Productivity Commission has been given an important job. Its role, expressed most simply, is to help governments make better policies, for the benefit of the Australian community. As its name implies, the Commission's focus is on ways of achieving a more efficient and productive economy — the key to higher living standards.

The Productivity Commission is an independent Commonwealth body, created by Act of Parliament in April this year, to replace the Industry Commission, the Bureau of Industry Economics and the Economic Planning and Advisory Commission (EPAC). It has been launched at a time of almost unprecedented debate about key policy directions for Australia. There has been a backlash against many of the policy reforms of the past decade, particularly those which have exposed Australian workplaces and regions to increased competition. And this reaction has spilled over to the institutions of government associated with that transformation.

The Productivity Commission's birth has accordingly been a protracted and difficult one. First signalled by John Howard in his 'headland' speech in the lead-up to the last election, the legislation forming the Productivity Commission had a protracted passage through Parliament. Along the way, it was steadfastly opposed by the Opposition, and various amendments were needed to obtain the eventual consent of the Senate.

Even before the *Productivity Commission Act* was passed, the Labor Party, at its conference in Tasmania in February, resolved to repeal it should it win power and replace the Productivity Commission with a 'National Development Authority'.

So it should be obvious that I am speaking to you today as the head of an organisation under some pressure. Still, it is hard to think of a time when that would not have been so — at least for the lineage from which the Productivity Commission's broad role and functions are largely derived. Indeed, some may recall that 25 years ago, the original legislation to create the Industries Assistance Commission (replacing the old Tariff Board) was also strongly opposed: only on that occasion the political roles were somewhat reversed — Labor was for it, the Country Party against.

Along the way, the previous Commissions went through some difficult times, facing strong opposition from sections of industry and the union movement, as well as within government itself. The institution found itself under threat of closure or emasculation on several occasions. At the same time, it had its supporters. They included some industry groups which did not always like its findings, but valued the transparency and consultative nature of its processes. And successive governments from both sides of politics have seen sufficient value in the institution to re-new and expand its mandate.

The Productivity Commission is the latest development in this process. It combines the strengths of the three organisations it replaced. It has new legislation which gives it a wider remit than any of its predecessors (though with a budget and staff one-third smaller). And it has already produced work which

demonstrates its potential to continue to assist public policy formulation. Yet it retains something of an image problem and it clearly has some powerful critics.

It would be foolish of me to presume that this simply ‘comes with the territory’, and that there was therefore nothing that we could do to enhance the Commission’s performance, or its acceptability to all sections of the community. On the contrary, I am conscious that we can do better in a number of areas.

But it would also be negligent of me to allow misunderstandings or misrepresentations of the Commission’s role and work to go unanswered.

So my purpose here is partly to set the record straight, but more importantly to explain how the Productivity Commission’s processes constitute a valuable resource for all governments.

The Commission’s ‘three pillars’

There are three core features of the Productivity Commission which together make it (and its Industry Commission predecessors) unique among public sector institutions in the world.

The first and most important of the three is its *independence*. The Commission operates under the protection and guidelines of its own legislation. It has an arm’s length relationship with government, which can tell it what to do — through inquiry references and requests for research — but not what to *say*. In a fundamental sense, the Commission reports not merely to the Government of the day, but to the Parliament and ultimately to the Australian community.

The corollary to this is that the Commission is only an advisory body — and only one source of advice at that. Its influence depends on the power of its arguments and the efficacy of its public processes. It makes recommendations to Commonwealth and State governments, but they are at liberty to accept or reject them.

The Commission’s independence is exercised formally through the Commissioners — who as statutory appointees cannot easily be removed. But its practical effect depends on the institution controlling adequate resources to undertake its work effectively, and on it being given worthwhile work to do.

The second of the Productivity Commission’s defining features is the *transparency* of its processes. The Commission’s advice, and the information it generates, are all open to public scrutiny. Its inquiries provide for extensive public input and interaction through hearings and other consultative forums, and the release of draft reports. This allows anyone with an interest to have a say, to respond to the views of others, and to comment on the Commission’s own preliminary views before it submits its report to government.

The third pillar underpinning the Productivity Commission is the obligation for it to take a *broad view*, encompassing the interests of the community at large. The policy guidelines in its legislation require the Commission to have regard to the need to “improve the overall economic performance of the economy.....to achieve higher standards of living for all members of the Australian community”. The Commission is also required to have regard to a range of more specific considerations, including the facilitation of adjustment to

change, the need to promote employment and regional development, and the social and environmental implications of its recommendations.

While there are potential tensions among some of its statutory guidelines, they collectively ensure that the Commission cannot put the interests of any particular group above those of the Australian community as a whole.

The Commission approaches its task of assessing the community-wide costs and benefits of policy in a variety of ways: by listening to those who may be affected and reviewing their evidence, and by analysing the effects in qualitative and quantitative ways, including through the use of economic modelling. At the end of the day, an element of judgment will generally be needed. And the outcome will not always coincide with the judgments of others. The fact that judgment is needed, however, is part of the reason why independence and transparency are important complements to the Commission's community-wide approach.

How it adds value

What this amounts to is an institution which can add value to public policy in two significant ways: first, through the nature of the advice it provides to governments, and second, through the informational and educative function of its processes.

From a government's perspective, it means that on key issues, it has available to it at least one source of information and advice that is well researched, impartial and concerned with the longer term interests of the community as a whole.

That is important, because although governments face no shortage of information and advice, much of it can be self-serving or too narrowly focused to allow for a broad or balanced assessment. This is obviously relevant to the claims of various industry or other pressure groups, but it can also apply to advice from line agencies within the bureaucracy — which typically have responsibility for a particular sector or group, rather than the broader community or the wider economy.

The Commission's processes can also help governments make the *right* decisions in the face of pressure from special interests to make the wrong ones.

For one thing, its reports provide facts and analysis for governments to draw on in communicating the need for change.

For another, the very process of public inquiry and research which produces our reports can play a useful role in promoting public awareness of the reasons why policy changes may be needed. In particular, it can alert those groups which would benefit from change and thus help to create a more neutral political environment for reform, which otherwise tends to be dominated by those whose interests are threatened.

The Commission's processes provide a convenient mechanism for even individual consumers and taxpayers to have a say.

Sometimes the main obstacle to agreement is simply lack of public knowledge about what is at stake. By unearthing the facts, the Commission's processes can contribute to a more focused and productive debate.

The Productivity Commission's first two reports, assessing the performance of Australia's waterfront, were generally seen as making that kind of contribution. Further opportunities are presented by (forthcoming) inquiries into the gambling industry and into the regional consequences of National Competition Policy. In both cases, the Government has recognised the value of the Commission's public processes in bringing into account the social as well as economic impacts of policy.

The Commission's public inquiries and research studies also provide the Government with an arm's length opportunity to test community reactions to different policy approaches. This can reduce the prospect of unanticipated responses which could stymie policy implementation. Examples include the Private Health Insurance inquiry — which looked at various modifications to community rating — and the current inquiry into Commonwealth funding of nursing homes in different states.

Such topics typify the Commission's special niche in the policy arena: those areas of policy characterised by conflicting interests — and thus significant political sensitivities — but with a potentially high payoff to the community from 'getting it right'.

Several streams of work

While public inquiries and other commissioned studies are the Productivity Commission's core business in this respect, it has several other streams of work which play an important but less widely recognised role.

One is performance monitoring — to help identify the need for policy action, to assess progress in implementing agreed reforms and to evaluate their effects. We do this via a secretariat role for inter-governmental committees monitoring the comparative performance of government enterprises (such as in transport or energy) and service provision (such as in health or education or community services). The information on government services is laying the foundation for each jurisdiction to provide better and more cost-effective service in areas which not only account for nearly 10 per cent of GDP, but are of central importance to community well-being.

Another mechanism, following on from the work of the BIE, is the international benchmarking of key infrastructure industries. This was the origin of one of our studies of the waterfront, and we are presently engaged in benchmarking Australia's telecommunications services.

The second waterfront report, on work arrangements in container stevedoring, was part of a broader stream of work on labour markets requested by the Government. We are currently engaged in similar research on work arrangements in meat processing and in the building and construction industries. The Commission's

draft report on the black coal industry also contained a detailed examination of work arrangements, which was drawn on in the AIRCs recent hearings on award simplification for that industry.

The Commission has an important ‘watch-dog’ role in regulation-making through its Office of Regulation Review — which must now be consulted on the impacts of all new Commonwealth regulation. This provides a new and important discipline on regulation-making, to ensure that it is necessary, well designed, and minimises costs to business. The Commission also houses a newly created Competitive Neutrality Complaints Office, to provide independent advice to the Treasurer on private sector complaints about unfair competition from the public sector.

We also have a mandate and the capacity to initiate additional research to ‘fill in the gaps’ and to prepare the way for future inquiries. In developing themes and topics for this general research stream, we conduct annual consultations with key interest groups and government departments. Themes for this year include the adjustment and regional implications of economic change, labour market flexibility and productivity, and impediments to better health services and aged care.

Shooting the messenger

As a catalyst for change in policy areas where there are often vested interests in maintaining the status quo, the Commission will often find itself in the firing line. Those who disagree with the Commission’s findings will naturally be tempted to shoot the messenger.

There have been three lines of attack recently. One accusation, carried over from the Industry Commission, is that the new body is ideologically driven. A related criticism is that the Productivity Commission, in combining three separate agencies, now monopolises policy advice. A third approach has been to dismiss the Commission as irrelevant because its advice has not been followed on some key issues.

Which ideology?

The first and most ingrained of these, that the Commission has an ideological antipathy to all forms of government intervention, probably has its origins in the protection debate under the former Industries Assistance Commission. While it is true that the Commission and its predecessors, including the BIE and EPAC, have been consistent in advocating reduced industry protection, this has had more to do with removing the costs on the Australian economy and community than with any ideological predisposition against government intervention.

Indeed, in its recent submission to the Mortimer review of business programs, the Commission outlined various circumstances in which governments needed to assist industry.

The Commission and its predecessors have also emphasised the value of competitive market disciplines to promote greater efficiency and productivity — and thus higher living standards. But this has not involved

doctrinaire adherence to unbridled market forces. Each case has been assessed on its merits. For example, in areas such as health and education, the Commission has emphasised the importance of mechanisms to ensure access for those on lower incomes. In a number of reports dealing with environmental issues, the Commission has supported government regulation to achieve better outcomes.

A careful, case-by-case assessment has also informed the Commission's approach to privatisation, which has generally been seen as of secondary importance to removing constraints on competition and advocated only where it would clearly bring additional benefits.

When one goes beyond industry assistance and public utility regulation to consider the other diverse policy areas in which the Productivity Commission now has a role, it becomes even more difficult to button-hole us. Yet the pattern, or lack of it, was already apparent under the Industry Commission. For example, can you find a common ideological basis for:

- the Commission's support for public provision of housing?
- its recommendations to maintain the 150 per cent tax concession for business R&D, or its strong support for basic research in universities?
- its advocacy of stronger duty of care enforcement for OH&S?
 - or the extension of the duty of care concept to land management regulation?
- its recommendation that the tax deductibility of donations to community social welfare organisations not only be retained, but extended?
- its rejection of unilateral open skies deregulation of international air services?
- its identification of the role of poor management practices as well as that of unproductive work arrangements in stevedoring?

I think you will agree that there is little evidence of an open slather free market ideology in these recommendations. Not only that, I suspect that most of them would not have been predicted by the participants in those inquiries — or even by the Commission itself at the outset. The fact is that most of our inquiries are a voyage of discovery. Where we end up depends on what we learn along the way.

Similarly, accusations that the Commission pursues a narrow concept of economics with little regard for adjustment or social issues have missed some important strands of its work. Some of our critics clearly have not read our reports.

There is a long tradition through the Commission's predecessors, of recommending phased or graduated change to allow time for orderly adjustment or to meet equity objectives.

A key instance is the consistent advocacy of gradual, predictable reductions in tariff levels, including in the most recent PMV and TCF reports. But there are many others. For example, while the Industry Commission's report on Urban Transport found that restrictions on taxi numbers were costing the public on average an extra \$2 a trip, it recommended that the restrictions be eased over a number of years by

auctioning additional plates, with the possibility of compensating existing licence holders with the sales proceeds. In its report on private health insurance, the Commission recommended modifications to community rating based on the age of entry, to help stabilise the system and make it fairer to long-standing members. It also proposed, however, that this change apply only to future entrants and that there be an initial grace period during which anyone could enter under the old rules.

In these and other inquiries, the Commission has generally given careful consideration to both the adjustment and distributional implications in making its policy recommendations.

For example, although not widely reported at the time, the TCF report identified a need to provide targeted support to improve the employability of workers needing language training and to ensure assistance to depressed regions where there is significant TCF activity. Emphasising the important role of generally available training and welfare programs in the adjustment process, the Commission recommended that the eligibility of any redundant workers for employment services should not depend on them receiving social security benefits.

Where the Commission has not recommended tailored support to facilitate adjustment by particular groups, this is not through any ideological objection, but because it has seen no additional pay-off from such schemes, which can be difficult to design and generally have a poor track record.

A concern for the effects of policies and policy changes on different groups of people and regions is embedded in the Productivity Commission's current research and inquiry program. But it was also evident in the work of the Productivity Commission's predecessors. For example, the Industry Commission documented the regressive incidence of import taxes (tariffs and quotas) and how some States benefited at the expense of others. More recent Commission research has explored the effects of a range of microeconomic reforms on employment in different industries and regions, and on the income levels of different socioeconomic groups. Such work has demonstrated that policy reforms have been only one among many pressures for change, often being outweighed by developments in technology and on international markets.

The Commission has also attempted to advance understanding of the social dimensions of microeconomic reform through published research, in its annual reports and community workshops — one example being its conference on 'equity, efficiency and welfare'. We can of course do more in this complex area and that is why it has a central place in our work program and our consultative processes.

I think all of this reveals the hollowness of accusations that the Commission's output is narrow in focus or predictably ideological. If we have one guiding principle, it is the community-wide perspective that we bring to our work. That is the real key to the diversity of the Commission's recommendations.

As already indicated, our findings and recommendations emerge from consultations with a wide variety of industry and community groups. To give a few examples, the Industry Commission inquiry into charitable organisations involved 220 visits to interested parties, 800 written submissions and 284 participants in

public hearings; the OH&S inquiry involved 250 visits and over 400 submissions; and the Land Management inquiry undertook 20 roundtable meetings, involving about 200 people across most regions of Australia. I expect the inquiries into the gambling industry and the effects of competition policy to involve more of the same.

The Commission can draw on a range of skills within the institution itself. Commissioners and staff have diverse backgrounds, qualifications and life experiences. The amalgamation of staff from the BIE, EPAC and IC enhanced this diversity, as did the appointment of new Commissioners. The *Productivity Commission Act* requires that there be Commissioners with extensive skills and experience in matters to do with the environment, social welfare delivery and the operations of industry.

This is supplemented by the appointment of Associate Commissioners with skills relevant to particular inquiries. Thus, the Industry Commission was fortunate to have had Sister Margaret McGovern from the Mercy Family Centre as an Associate Commissioner in the Charitable Organisations inquiry; Michael Easson, with his union background, on the inquiry into OH&S; Prof Mick Common from ANU's Centre for Resource and Environmental Studies on the Greenhouse inquiry, and so on.

Such part-time appointees enrich the Commission's understanding of the issues and enhance the credibility of its judgments. They obviously also need to share the requirement on permanent Commissioners that there be no conflicts of interest which could be seen as affecting their judgment. This has been highlighted by the recent designation of the Productivity Commission as Australia's authority for hearing claims for temporary import protection under the safeguards provisions of the WTO. Any doubts about the impartiality of those processes in the current pigmeat case, for example, would put Australia at risk of subsequent challenge in Geneva.

The Commission also has the flexibility to draw on the expertise of others in a variety of ways, including through external consultancies and staff secondments. These mechanisms are widely used.

But we can always do better. In the Gambling Inquiry, for example, we intend to form a consultative panel of eminent people with a range of social and industry perspectives, to generate and test ideas and provide constructive feedback.

Indeed, I see value in extending this concept by developing broader consultative mechanisms for the Productivity Commission as a whole. Forums involving leading industry and community representatives could play a valuable continuing role in helping the Commission understand how it can do its job better, as well as enhancing public understanding of its approach. One such consultative mechanism already exists, to help shape the Commission's research program.

Monopolisation of advice?

There has been some criticism that creating the Productivity Commission through the amalgamation of three separate agencies has diminished the competition for ideas and the breadth of views available to government.

It is undeniable that there are now fewer such government organisations than there were before, and this will inevitably have some effect. But this needs to be put in perspective.

For one thing, the key functions of each agency have been preserved in the Productivity Commission. For example, in addition to the public inquiry activity of the IC, the BIE's international benchmarking of economic infrastructure is continuing — as evidenced by our recent waterfront report — and EPAC's concern with social issues is a core feature of the new Commission's program. Moreover, there is now a more widely ranging research program than existed under the separate agencies. Much of this work is published as staff papers.

It is also possible to exaggerate the separate contribution of the three agencies. In recent years, there was considerable commonality in their findings and conclusions in those areas where their work overlapped, which it increasingly did.

Governments have available to them many other sources of advice.

The Productivity Commission could scarcely be regarded as having a monopoly within the public sector. The policy departments (such as DIST or DEETYA or Prime Minister and Cabinet) are all very forthcoming in presenting their views to Ministers, as of course are Ministers' own offices. And most Commonwealth departments have a substantial research capability as well, or could build it (or contract it) if they chose.

It is also misleading to lump the Productivity Commission in with the Treasury as is sometimes done. Although the Commission reports to the Treasurer, it is quite separate from the Treasury department and has its own independent voice.

The Commission must also compete with the wide-ranging sources of advice from private sector consultancies and think tanks, such as the Centre for Independent Studies, Evatt Foundation, Institute for Public Affairs, Access Economics, Centre for International Economics, ACIL and the many other 'centres' now proliferating at our universities. Then there are the myriad lobbyists and organisations representing particular industries and community interests, as well as individual companies.

If anything, the Productivity Commission's public inquiry processes *facilitate* the competition for ideas among these many parties, whose influence may otherwise be exercised behind closed doors and never be adequately tested.

This also suggests why the Productivity Commission's role could not simply be privatised or contracted out. Its critical distinguishing characteristics of independence, transparency and a community-wide perspective constitute what is fundamentally a public good, which government itself needs to establish.

Governments can and do set up *ad hoc* committees of inquiry or review on key issues. And there has been a variety of them in recent times. Their contribution depends very much on how they are constituted and resourced and whether they can exercise an effective independent role. Some recent ones in the industry

policy domain have performed poorly against such criteria; others, like the recent review of the financial system, have performed very well.

How influential?

One potential liability for government in sending references to the Commission, especially on issues where the political stakes are high, is that it will not always like the answer. To be true to its charter, the Commission needs to look at issues on their merits, against economy-wide tests, without second-guessing the politics. It can of course provide options for governments to consider, but needs to be clear about the basis for its preferences. This inevitably means that the Commission's advice will not always be accepted.

It would be misreading the Commission's role, however, to interpret any rejection of its advice as indicating that the institution is of no value to the policy-making process.

A government must make policy decisions based on a range of considerations, including its judgment about what will be acceptable to the public and about the appropriateness of the timing. The Commission's advice is but one input among many to the eventual outcome. Because it is independent and directed at the long-term public interest, it nevertheless plays a significant role in helping governments understand the tradeoffs in different policy choices.

The fact that a government may not initially accept key recommendations in a particular report does not mean that that report has no influence. If we take the PMV and TCF reports as the most relevant recent examples, a number of the findings and recommendations in both reports were in fact accepted by the Government. And, although the Commission's majority positions on the rates of tariff phase-down were rejected, both the Government and industry agreed to further reductions after the current programs are completed in the year 2000. It is reasonable to ask whether this could have been achieved in the absence of those inquiries. I think not. Indeed, the political pressures building at that time were such that we could well have gone in the opposite direction.

It is also not uncommon for recommendations to be acted on some years later. This may be triggered by a change in government or in the economic climate, or just greater public acceptance of new ideas with the passage of time. The general program of phased tariff reductions which commenced in 1988 under the Hawke government, owed much to a 1981 report on approaches to general reductions in protection on which the Fraser government took no action. A more recent example is the Government's deregulation of the petroleum industry, which was broadly in line with the recommendations of the Industry Commission's 1993 report.

Indeed, it is a measure of the Commission's independence from the government of the day that its reports are often sought by opposition parties as a source of ideas for their own platforms.

Thus it was interesting to observe the Opposition's use of the Industry Commission's R&D report to support its position on that topic, in a document which also outlined plans to abolish its successor.

A final perspective on the Commission's influence, which has its own irony, is the steady demand for its reports from international agencies and foreign governments. To provide a first-hand illustration, I was recently invited to address a conference on private health insurance in Ireland, where I was astonished to find our report being described as a key input to the current review of that country's own health insurance system. Among other examples, the Industry Commission's pioneering work in measuring industry assistance has been picked up by the WTO and APEC and is now adopted in many countries. Our approach to regulation review has been embedded in OECD codes for member governments. And the Commission itself has been advocated as an institutional model for other countries by international agencies concerned with policy reform.

In conclusion...

The Productivity Commission is getting on with an extensive program of work, ranging across policy areas of long-term importance to the community. While it has the advantage of well-established processes of transparency and independence, the Commission's output will also be shaped by its new legislation and appointments. These have served to broaden its perspective further and have brought greater emphasis to the adjustment and social dimensions of structural reforms.

Recent political developments demonstrate the importance of dealing effectively with these issues, if generally beneficial policy changes are to proceed. When people are doing it tough and there is mounting pressure for piecemeal policy responses and quick fixes, it is particularly important that we as a society can maintain the basis for a properly informed debate.

I believe that the Productivity Commission's role is integral to this process. While its findings will rarely please everybody, they have the benefit of a robust consultative process in which the interests of the wider community are the dominant consideration.